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C O N F I D E N T I A L SECTION 01 OF 02 JEDDAH 000508

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SUBJECT: KING ABDULLAH ECONOMIC CITY: BRAVE IDEAS, SHAKY
SAND

Classified By: Consul General Tatiana Gfoeller for reasons 1.4 (b) and
(d).

1. (C) SUMMARY: Nearly two years after the launch of construction, the King Abdullah Economic City (KAEC) remains the flagship among the megaprojects that represent King Abdullah's push for modernization and economic diversification. Although the King's support for the city still appears strong, construction delays highlight the implementation challenges facing such projects within the Kingdom. It is also uncertain whether KAEC, once completed, can attract sufficient participation from the multinationals and professionals that the city is designed to aggregate.
END SUMMARY.

THE VISION

2. (U) 90 miles north of Jeddah, KAEC will be the largest of six "economic cities" that are being developed as catalysts for modernization and economic diversification. The city, planned for completion in 2016, will occupy 65 square miles and comprise six zones: industrial, financial, educational, resort, residential, and seaport. The city's layout and infrastructure are designed to encourage interaction between the zones.

3. (U) Although the core activity of all six economic cities will be based on Saudi Arabia's comparative advantage of low-cost energy, they are meant to diversify the Kingdom's economy by creating jobs in the downstream petrochemical sector and in non-oil industries. According to the Saudi Arabian General Investment Authority (SAGIA), KAEC has the potential to create one million jobs, many of them high-skilled. The hope is that these will eventually be filled by Saudis, thereby promoting the SAG's Saudization policy.

STILL A MIRAGE

4. (C) On a visit to the KAEC site on October 27, EconOff saw that construction progress to date included a stylish sales center and several lavish sample villas on the shoreline. These structures were surrounded by miles of open desert dotted by intermittent earth-moving projects such as grading and canal digging. Saleh Saadawi, the senior on-site construction manager, said that the King recently made a surprise inspection and was angry at the apparent lack of progress. Management had responded by adding workers and keeping full labor shifts rather than cutting back in observance of Ramadan.

5. (C) Mr. Saadawi attributed the slow progress largely to the difficulty of hiring a Saudization-compliant workforce,

saying that there are not adequate numbers of Saudis willing to work in the construction trades. He also said that there have been significant cost overruns due to the rising prices of services and materials, which he attributed to the global building boom. Even Chinese subcontractors, traditionally some of the least expensive, are becoming significantly more costly.

¶6. (C) Asked about the number of U.S. companies involved in KAEC, Mr. Saadawi named Parsons International, the planner for the city's industrial zone, but said he did not understand why more U.S. firms were not bidding on contracts.

(Note: Commercial Consul told EconOff that U.S. companies who decline to work in the Kingdom often cite their insurance providers' non-coverage of employees due to security concerns. End note.) Mr. Saadawi said although U.S. firms tend to be more expensive than the global competition, they are known within the region for a high level of quality and service that is, in his opinion, often worth the price.

IF YOU BUILD IT, WILL THEY COME?

¶7. (C) The success of KAEC depends not only on its timely construction but on its ability to attract the participation of investors and tenants. Emaar the Economic City (EEC), the consortium developing the project, held an initial public offering which was oversubscribed in just three days, indicating strong investor confidence. It remains to be seen whether a critical mass of corporations will be willing to invest directly in the city by building offices and plants there.

¶8. (C) Even with a significant commitment from international

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corporations, the city will face challenges in creating jobs.

The industries to which KAEC will cater tend to be capital-intensive rather than labor-intensive, restricting the scale of any new employment. Nor is it clear that the Saudi educational system can produce a significant portion of the high-skilled workforce that KAEC is meant to employ. The Kingdom's ability to develop more advanced industries is also limited by weak protection of intellectual property rights and by continued state dominance of the economy.

¶9. (C) EEC executives told EconOff they are optimistic about the SAG's intent and ability to address these structural concerns, and are particularly convinced of King Abdullah's commitment to economic reform. They cited the planned King Abdullah University of Science and Technology (KAUST), adjacent to KAEC, as evidence of the King's desire to create a highly skilled Saudi workforce. They also said that KAEC itself will help generate skilled workers through the undergraduate facilities within its education zone, which is to be tightly integrated with the financial and industrial zones.

LIMITED SPEED, LIMITED TIME

¶10. (C) As with his other initiatives, the octogenarian King must make the most of the time he has without pushing for change so aggressively as to encourage a conservative backlash. Dr. Ghazi Binzagr, a Jeddah-based executive who advises the SAG on economic reform, told EconOff that the monarch is in a race against time to initiate the modernizing projects that will be his legacy, and added that whoever succeeds him may not have the appetite or ability to continue this course.

¶11. (C) In addition to giving KAEC political cover, the King may be providing the essential vision for the project. Dr. Binzagr told EconOff that much of the public excitement generated by KAEC stems from locals' desire to "look like Dubai," and that it is easy to mistake impressive real estate

for meaningful progress. However, in Dr. Binzagr's estimation, the King understands that the city's key contribution should be the human capital that it is designed to nurture.

AN IRRESISTIBLE FORCE MEETS AN IMMOVABLE OBJECT?

¶12. (C) COMMENT: The King's support for megaprojects like KAEC and the accompanying institutional reforms is significant in a country whose natural resources have long allowed it to sidestep economic and cultural change. The oil-generated wealth available to fund these projects is at an unprecedented level, as is pressure from the investor and professional classes to modernize the culture and liberalize the economy. Nevertheless, it is not yet clear that these forces can overcome the combined inertia of the Kingdom's conservative culture, its powerful religious establishment, and an educational system that is still not matched to the vision that inspires the economic cities. END COMMENT.
GFOELLER